Tax-Exempt Private Activity Bonds

Tax-exempt financing of "private activities" has been limited by federal law since the passage of the Tax Reform Act of 1986 (the "Tax Act"). Private activity bonds are those which have met any or all of the following tests:

1) **Private Business Use Test** - more than 10 percent of the bond proceeds are to be used for any private business use;
2) **Private Security or Payment Test** - payment on principal or interest of more than 10 percent of the proceeds is directly or indirectly secured by, or payments are derived from, a private business use; and
3) **Private Loan Financing Test** - proceeds will be used to make or finance loans to persons other than governmental units.

The Tax Act also restricts the types of privately-owned public purpose projects which can take advantage of tax-exempt financing. The types of issues authorized, which are relevant to this section, are mortgage revenue bonds (MRBs), small-issue industrial development bonds (IDBs), student loan bonds, and those for a variety of "exempt facilities", including qualified residential rental projects (multi-family housing), sewage facilities, solid waste disposal facilities, and hazardous waste disposal facilities.

Additionally, the Tax Act imposes a volume ceiling on the aggregate principal amount of tax-exempt private activity bonds that may be issued within each state during any calendar year. Washington State’s 2005 ceiling is equal to $80 per capita or $496.3 million.